FILED
AUG 28 1944
CHARLES ELMORE CROPLEY
CLERK

Supreme Court of the United States

OCTOBER TERM, 1944

No. 408

CLOVER SPLINT COAL CO., INC.,
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT AND BRIEF IN SUPPORT THEREOF.

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THE SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1944

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Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE
Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

To the Honorables, the Chief Justice and the Associate Justices of the Supreme Court of the United States;

Your petitioner, Clover Splint Coal Co., Inc., a corporation, respectfully prays that a writ of certiorari issue to review the final order and decision of the United States Circuit Court of Appeals for the Third Circuit, entered on the 6th day of June, 1944, affirming an order of The Tax Court of the United States, finding that there were deficiencies against this petitioner in income taxes in the respective principal amounts of $6,528.51 and $6,064.60 for the calendar years 1938 and 1939, re-

spectively. An order has been entered staying the mandate pending this application.

OPINIONS BELOW
(Record)

There is presented with this petition a certified transcript of the record in the case, including the proceedings in the court to which the writ is asked to be directed. Included in such transcript is the printed record, consisting of appendix to the brief of petitioner filed in the Circuit Court of Appeals, and references to the record herein set forth are to the pages of such printed record. There is filed with this petition stipulation of counsel for petitioner and respondent that subject to the approval of the Court such appendix and proceedings in the Circuit Court of Appeals may constitute the printed record upon this petition. The memorandum, findings of fact, and opinion of The Tax Court of the United States appear at pages 62-a to 64-a, inclusive of the printed record, and the opinion of the Circuit Court of Appeals not yet officially reported appears in the transcript of the record.

JURISDICTION

The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925 (Chap. 229, 43 Stat. 936, 28 U.S.C.A. 347).

STATUTE INVOLVED

The issues involve the construction and application to the facts of this case of Section 114(b)-4 of the Act of Congress approved June 22, 1936, known as the Revenue Act of 1936, which reads as follows, those portions

thereof especially pertinent to the determination of this matter being italicized by us:

"(4) PERCENTAGE DEPLETION FOR COAL AND METAL MINES AND SULPHUR.— The allowance for depletion under section 23 (m) shall be, in the case of coal mines, 5 per centum, in the case of metal mines, 15 per centum, and, in the case of sulphur mines or deposits, 23 per centum, of the gross income from the property during the taxable year, excluding from such gross income an amount equal to any rents or royalties paid or incurred by the taxpayer in respect of the property. Such allowance shall not exceed 50 per centum of the net income of the taxpayer (computed without allowance for depletion) from the property. A taxpayer making his first return under this title in respect of a property shall state whether he elects to have the depletion allowance for such property for the taxable year for which the return is made computed with or without regard to percentage depletion, and the depletion allowance in respect of such property for such year shall be computed according to the election thus made. If the taxpayer fails to make such statement in the return, the depletion allowance for such property for such year shall be computed without reference to percentage depletion. *The method, determined as above, of computing the depletion allowance shall be applied in the case of the property for all taxable years in which it is in the hands of such taxpayer, or of any other person if the basis of the property (for determining gain) in his hands is, under section 113, determined by reference to the basis in the hands of such taxpayer, either directly or through one or more substituted bases, as defined in that section. The above right of election shall be subject to the qualification that this paragraph shall, for the*

purpose of determining whether the method of computing the depletion allowance follows the property, be considered a continuation of section 114 (b) (4) of the Revenue Act of 1934, and as giving no new election in cases where such section would, if applied, give no new election."

STATEMENT OF THE CASE

There is here involved no dispute of fact, and the facts will be found summarized in the opinion of the Court of Appeals and in that of The Tax Court, page 62-a of the printed record.

Clover Splint Coal Company is a West Virginia corporation, keeping its books and filing its tax returns for the calendar years 1938 and 1939 in the office of the Collector of Internal Revenue at Pittsburgh, Pennsylvania. For some years prior to 1934, it operated a coal mining lease in Kentucky. In each of the years 1934 and 1935 it had substantial net losses (see Exhibit Tax Returns), and on its returns for those years it made no election with respect of percentage depletion. In the year 1936 it had a small net income and first elected percentage depletion in its first return for that year. In 1938 and 1939 it made claims for deduction of depletion on the percentage basis, which were disallowed by the Commissioner of Internal Revenue, respondent in this case, resulting in the deficiencies as heretofore set forth in income and excess profits taxes for the years in question. No part of the above amounts claimed for depletion were allowed upon a cost basis. (Printed Record page 52-a). Taxpayer at all times operated under a lease (Exhibit 1-A, printed record, page 53-a), and it has at all times remained the lessee thereunder (Printed Record, page 51-a).

QUESTIONS PRESENTED AND ERRORS URGED

(1) Whether petitioner was entitled to a depletion allowance in the years in question by reason of having elected percentage depletion upon its first return for the year 1936, the latter being the first year in which it had net income from which depletion allowance could be deducted.

(2) Whether the Act of 1936 gave a new election except in cases of change in ownership, it being taxpayer's contention that, by the terms of the latter part of Section 114(b)-4, said act was an extension of prior acts *only for the purpose of following the property in the case of transfer*. The refusal of the Court below to hold that the Act of 1936 gave taxpayer a new election, there being no transfer of taxpayer's property, is urged as error.

REASONS RELIED ON FOR ALLOWANCE OF THE WRIT

(1) The Circuit Court of Appeals has decided an important question of Federal Law, which is not, and should be, settled by this Court in that,

(a) The interpretation of Section 114(b)-4 of the Revenue Act of 1936, and similar language in other Revenue Acts has been before this Court with respect of the first part of said section, particularly as to the meaning of "first return", but the later language of said section with respect of its being a continuation of prior acts for the purpose of following the property, has not been interpreted by this Court and is a matter of great interest involving operation of a general tax law in situations often likely to arise; and

(b) The interpretation so given by the Cir-

cuit Court of Appeals to the latter part of said section in the present case is inconsistent with the rules of interpretation applicable to this section, laid down by this Court.

(2) The decision of the Circuit Court of Appeals is substantially in conflict with the decisions of this Court on a matter of great public interest, in the following particulars:

(a) At the time of the filing of the petition in The Tax Court of the United States, the Circuit Court of Appeals of the Third Circuit had given a so-called liberal interpretation to Section 114(b)-4 in two cases to be hereinafter discussed, holding (1) that an election of percentage depletion was not necessary until taxpayer had net income from which the deduction might be made of depletion allowance and that the expression "first return" used in the statute was to be construed, not with its literal meaning, but to effectuate an assumed intent of Congress; and (2) that while the literal meaning of the latter part of the statute would limit its operation to cases where there had been a transfer of property, such literal meaning would be disregarded as being against the assumed intention of Congress, and the Act held a continuation of prior acts for all purposes.

This Court, in cases discussed in the brief accompanying this petition, has held that a strict interpretation must be applied to the words "first return" and an election made in the "first" year regardless of whether there was net income, a strict construction that logically must be applied throughout the section in question. Never-

theless, the Circuit Court of Appeals in the instant case adhered to its rule of liberal construction of the latter part of the section, and accordingly, there is an inconsistency whereby (a) under the rule of strict construction, the first contention of taxpayer is denied; and (b) under the liberal construction of the same section of the statute, taxpayer's second contention is denied. There is, accordingly, involved a question of inconsistency in the interpretation of an important Federal Statute applicable in numerous cases.

WHEREFORE, your petitioner prays that a writ of certiorari be issued out of and under the seal of this Honorable Court, directed to the Circuit Court of Appeals for the Third Circuit, commanding that Court to certify and send to this Court for its review and determination on a day certain to be named therein, a full and complete transcript of case numbered on its Docket No. 8125, and entitled Clover Splint Coal Company, Inc., Petitioner, Appellant, v. Commissioner of Internal Revenue, Appellee, and that the judgment of the Circuit Court of Appeals for the Third Circuit entered on June 6, 1944, may be reversed, and the decision of The Tax Court of the United States entered on June 30, 1943, may be reversed, and this petitioner held not liable for the taxes in question, and that this petitioner may have such other and further relief in the premises as to the Court may seem proper.

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OCTOBER TERM, 1944

No.....

CLOVER SPLINT COAL CO., INC.,
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vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

STATEMENT

Reference to the opinion below, a statement of the grounds upon which the jurisdiction of the court is invoked, and a statement of the case, under appropriate headings, are set out in the foregoing petition, and to avoid duplication are not repeated here.

SUMMARY OF ARGUMENT

A unique situation is here presented in which any consistent interpretation of Section 114(b)-4 of the Revenue Act of 1936 will necessarily result in sustaining one or the other of taxpayer's two contentions. At

the time petition was filed before the Tax Court (Board of Tax Appeals), the Circuit Court of Appeals for the Third Circuit in two decisions had adhered to a literal interpretation of the section in question. In the case of *Pittsburgh-Duryea Coal Co.* v. *Commissioner*, 117 F. 2d 436, it was held that a taxpayer need not elect percentage depletion until the year in which it first had a net income, the literal reading of the words "first return" contained in the statute being rejected. In *Tonopah Mining Co.* v. *Commissioner*, 127 F. 2d 239, it was held that while a literal meaning of the latter part of Section 114(b)-4 of the Act of 1936, would make such act an extension of prior acts only in the case of transferred property, such literal meaning would not be followed.

The doctrine of the *Pittsburgh-Duryea* case, as counsel frankly admit, can no longer stand in view of *Mother Lode Coalition Mines Co.* v. *Helvering*, 317 U. S. 222, 87 L. ed. 227, but the Court of Appeals refused to recede from the doctrine in the *Tonopah* case, with the result: (a) The first contention of taxpayer originally made before the Tax Court is denied under the rule of *strict* construction, a literal meaning being given to the words "first return" as used in the statute, and (b) the second contention of the taxpayer is denied under the rule of *liberal* construction, the words in the statute with reference to Section 114(b)-4 being an extension of prior acts "for the purpose of determining whether the method of computing depletion allowance follows the property" being denied their literal meaning.

ARGUMENT

A consistent interpretation of the section should be given. If the section were liberally construed, taxpayer

would prevail under its first contention. If it be literally construed, taxpayer must prevail under its second contention.

INTERRRETATION OF THE STATUTE

At the time this appeal was filed with the Tax Court the validity of petitioner's first contention that it was entitled to a new election in 1936, because such was the first year in which it had a net taxable income, had been upheld by the Circuit Court of Appeals in *Pittsburgh-Duryea Coal Co.* v. *Commissioner*, 117 F. 2d 436. That Court gave a liberal interpretation to the section in question, refusing a literal reading thereof, saying on page 438 of the opinion:

> "Further, 'statutes must be construed in the light of their purpose. A literal reading of them which would lead to absurd results is to be avoided when they can be given a reasonable application consistent with their words and with legislative purpose'. Haggar Co. v. Helvering, 1940, 308 U. S. 389, 394, 60 S. Ct. 337, 339, 84 L. ed. 340. We think it would be an absurd result to construe this statute to require the taxpayer to choose a method of depletion and to state the method when there is nothing from which to make the deduction."

The effect of *Mother Lode Coalition Mines Co.* v. *Helvering*, decided by this Court on December 7, 1942, is later considered.

Prior to the *Mother Lode* case, however, the second question here present came before the Court of Appeals in *Tonopah Mining Co.* v. *Commissioner*, 127 F. 2d 239, decided on March 17, 1942. This case involved pre-

cisely petitioner's second contention and the Court recognized that the literal meaning of the qualification clause of the Act of 1936 would make it applicable only where there was a change of ownership, such recognition being clearly set out on page 244 of the opinion in the following language:

> "A literal meaning of these words implies that the sentence is inapplicable unless there has been a change of ownership."

Such, of course, is the only possible literal reading of the language in question, as it specifically states that the right of election is only subject to qualification *"for the purpose of determining whether the method of computing the depletion allowance follows the property."* Fully recognizing that a literal reading of the statute would render it applicable only where there was a change of ownership, the Court of Appeals, following in principle the *Pittsburgh-Duryea* case, refused to give such liberal interpretation, saying:

> "But such a result would be absurd. It would allow those who retained ownership after 1934 to elect anew, while binding those who took as successors in interest."

The Court continues:

> "If we are to avoid this curious result, what meaning is to be attached to the words 'follows the property'?"

In avoidance of such literal meaning the Court assigns a "contextual" meaning to the sentence, as if the words "through the years" came directly after "follows the property", making the words "follows the property"

synonymous with "adheres to the property". The conclusion of the Court is:

> "Since the literal meaning leads to an absurd result, it must be rejected in favor of a contextual meaning which accords with the legislative intent."

It will be noted that the following steps are taken by the Court: (a) It is stated that the literal meaning of the sentence in question would make it applicable only in case of transfer; (b) such would lead to an "absurd" result presumably contrary to the intention of Congress; and (c) to avoid this "curious result" words are to be inserted in the statute and a conclusion reached admittedly contrary to the literal meaning.

What is the result of this "contextual" interpretation? The opinion of the Court of Appeals states that such effect is to make the words "follows the property" synonymous with "adheres to the property". Such, of course, has the effect of making the paragraph apply to all property whether transferred or not and of making the act generally a continuation of the Act of 1934. So interpreted, the words become absolutely needless and meaningless, and the paragraph would operate as though the whole of the qualification section were omitted. Without it the section would read (asterisks showing omissions):

> "* * * this paragraph * * * shall be considered a continuation of Section 114(b) (4) of the Revenue Act of 1934, and as giving no new election in cases where such section would, if applied, give no new election".

If Congress had intended that the Act of 1936 should

be a general continuation of the Act of 1934, without qualification, it would have used such language. There would have been no reason for any qualification clause. The "contextual" interpretation of the Court as is most deferentially submitted, results in excising the qualification clause from the statute, depriving it of all function, no less effectually than if the clause were disregarded without explanation. Being in the statute, it may not be disregarded.

It is obvious that the position of the Court of Appeals in the *Tonopah* case and the instant case is diametrically opposed to the position taken by this Court in the *Mother Lode* and *Riley Investment Company* cases. Furthermore, it is to be emphasized that the part of Section 114(b) (4) immediately preceding the words in question deals with a transfer of property where the basis of such property is (under Section 113) determined by reference to the basis of a prior taxpayer. It is, therefore, clear that Congress had in mind a transfer when it inserted the words "follows the property" in the last sentence. However, even if the words were not used in this connection, their literal meaning is clear. They import a transfer of property.

It will, therefore, be noted that in both the *Pittsburgh-Duryea* case and the *Tonopah* case the Court of Appeals gave a consistent, liberal interpretation to the statute to avoid "absurd results", that precisely identical expression being used in both opinions. However, this Court gives a strict interpretation to the statute, not only in the *Mother Lode* case but in *J. E. Riley Investment Co.* v. *Commissioner*, 311 U. S. 55, 85 L. ed. 36. In the latter case this Court frankly says that there may be basis for an appeal to Congress in

amelioration of the "strictness of that section", but such is for Congress. A strict construction had been characterized in the *Tonopah* case as "absurd" if it allow those who retained ownership of a property after 1934 to elect anew, while binding those who took as successors in interest, and, with almost the same language, the Circuit Court of Appeals had spoken of the same conclusion later reached in the *Mother Lode* case as "an absurd result". It is plain that this latter thought is fully answered in the *Mother Lode* opinion, but the same answer applies to the reasoning of the *Tonopah* case. Where language is clear, there is no room for construction, and the result that may follow in the application of a statute is a congressional, and not a judicial, responsibility. If the Act of 1936 be an extension of the Acts of 1934 and 1935, so that no new election may be given in any case, the underlined words of the statute are absolutely meaningless:— "The above right of election shall be subject to the qualification that this paragraph shall, *for the purpose of determining whether the method of computing the depletion allowance follows the property,* be considered a continuation of section 114(b) (4) of the Revenue Act of 1934, and as giving no new election in cases where such section would, if applied, give no new election." These words are used in the statute following language showing that Congress had in mind substituted bases in the case of transfers. They constitute, without ambiguity, a definite limitation of the extension provision of the statute. In such case it is not for a court to speculate as to legislative purpose. It may well have been that Congress desired to penalize the recipients of tax free transfers as contrasted with those who continued to hold property. However, such speculation is here beside the point for the words of limitation are specific and unambiguous. The

Act of 1936 is a general tax law, giving a new right of election except in those cases in which the limited provision extending the prior act is operative, and such extension is only to follow the property in the case of transfer.

A fundamental rule of statutory interpretation is that words of clear import may not be disregarded, and effect shall be given to every clause and part of a statute in the absence (as here) of irreconcilable inconsistency.—*Ginsberg & Sons* v. *Popinkin*, 283 U. S. 204, 76 L. ed. 704. Here, there is no difficulty in giving effect to the words in question. The position of the Circuit Court of Appeals may be fairly stated, we believe, as follows—while the words are there and their literal meaning is recognized in the *Tonopah* case, the Court weighs and rejects the *results* that would spring from giving them effect. If these words be disregarded, it is most respectfully submitted that the process is one not of *interpretation* by a court, but of *elimination* of statutory words, with attendant change in the scope of the statute itself.

It is most respectfully submitted that the court below has failed to recognize the issue here involved. It is stated in the opinion below that there was a "common sense" interpretation of the statute, designed to effectuate the plain intent of the Legislature in both the *Mother Lode* and *Tonopah* cases. Certainly no quarrel is taken with that statement as applied to the *Mother Lode* opinion where this Court points out the practical difficulties that would follow from other than a strict interpretation of the expression "first return", the necessity of keeping all returns open in order later to check depreciation and deductions, etc. The result in the

Mother Lode case is arrived at by giving full and certain effect to the wording of the statute, and the same is true of the *Riley Investment Company* case; but the statutory interpretation in the *Tonopah* case involves *elimination* of statutory words which definitely limit the purpose and scope of the statute itself. The Court states that petitioner's complaint is really of the "strictness" of the section as stated in the *Riley Investment Company* case. It is respectfully submitted with all deference that if the "strictness" of the section be invoked consistently taxpayer must prevail. It is not really, however, necessary to invoke so strict a construction as that in the *Riley Investment Company* case, because unless the words "for the purpose of determining the method of computing depletion allowance follows the property" be absolutely disregarded, eliminated through judicial excision, taxpayer must prevail. Such will produce no harsh results such as are referred to in the *Riley* case. Congress had a right to extend the Act of 1934 in cases of transfer with substituted bases in the hands of the transferee, and not extend that act in cases of properties held without transfer. Its purpose in so doing is not a matter of judicial question but even if the results were harsh, this Court will follow the statutory language.

Reference is again made to the *Riley* case, in which this Court stated that any harsh results that might follow the decision were a matter for Congress, and, a fortiori, it follows that if Congress were ill advised in limiting the extension provisions of the section in question, the correction of that policy is with Congress and not with the courts.

This Court has been consistent in upholding the doc-

trine here contended for. The case of *Scaife* v. *Commissioner*, 314 U. S. 459, 86 L. ed. 339, arose under the capital stock tax law, but strongly fortifies the contention of petitioner. The Court says in upholding a literal reading of the statute:

> "The result in individual cases may be harsh. But that may be true in case of any statute of limitations. As we indicated in J. E. Riley Invest. Co. v. Commissioner of Internal Revenue, supra, such considerations, though a basis for an appeal to Congress for relief in individual cases are not appropriate grounds for relief by the courts from the strictness of the statutory demand."

See also *Helvering* v. *Lerner Stores Corp.*, 314 U. S. 463, 86 L. ed. 343.

There is here present an obvious injustice to the taxpayer. However, a larger question is presented: A section of the Revenue Act has been inconsistently interpreted, whereby two statutory interpretations have been invoked, basically different in underlying philosophy, and applied to the same section. If the present status of precedent were not corrected by this Court the anomalous situation would be presented of Section 114(b)-4 of the Revenue Act of 1936, (and the corresponding provisions of other acts up to 1942) being interpreted strictly (under the decisions of this Court), except as to its later provisions. In the *Tonopah* case and this case, the holding of the Circuit Court of Appeals of the Third Circuit is "liberal" to the point of eliminating statutory language, as is most respectfully submitted.

CONCLUSION

It is respectfully submitted that this is a case in which the court, in its sound judicial discretion, may appropriately grant the writ of certiorari prayed for, and that the petition and the brief in support thereof present special and important reasons therefor.

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In the Supreme Court of the United States

OCTOBER TERM, 1944

No. 408

CLOVER SPLINT COAL CO., INC., PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The memorandum findings of fact and opinion of the Tax Court of the United States (R. 62a–64a) are unreported. The opinion of the United States Circuit Court of Appeals for the Third Circuit (R. 70–73) is reported in 143 F. (2d) 108.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on June 6, 1944 (R. 73–74). The petition for a writ of certiorari was filed on August 28, 1944. The jurisdiction of this Court

is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

The petitioner failed to elect to take coal percentage depletion in 1934 and thereby elected negatively to take depletion deductions in that and subsequent years on the cost basis under Section 114 (b) (4) of the Revenue Act of 1934.

The question is whether the petitioner was entitled to a new election for the years 1938 and 1939 either under Section 114 (b) (4) of the Revenue Act of 1936 or under Section 114 (b) (4) of the Revenue Act of 1938.

STATUTES AND REGULATIONS INVOLVED

These are found in the Appendix, *infra,* pp. 11–16.

STATEMENT

So far as material here, the facts found by the Tax Court may be summarized as follows:

On February 26, 1927, the petitioner, a West Virginia corporation, acquired a coal mining lease in Harlan County, Kentucky, at no cost, and has at all times since remained the lessee thereunder (R. 62a). In its returns for 1938 and 1939 the petitioner claimed a deduction on account of percentage depletion in the amounts of $37,700.76 and $34,922.63, respectively (R. 62a).

The petitioner did not in its return for the years 1934 and 1935 indicate its election to compute deductions for depletion on the percentage basis, but it did make a statement in its return for 1936 to the effect that it elected to have such allowance "computed with regard to percentage depletion" (R. 63a).

It further appears from the record that the petitioner had gross, but no net, income in 1934 and 1935 (R. 25a, 41a), and it is stated in the opinion of the Circuit Court of Appeals that the petitioner's return for 1936 disclosed a small net income (R. 72).

The Commissioner disallowed the claim (R. 14a, 16a–17a). He accordingly determined deficiencies for the taxable years 1938 and 1939 in the amounts of $6,528.51 and $6,064.60, respectively, which resulted primarily from the disallowance of such claims (R. 15a–16a, 20a–21a). The Tax Court sustained the Commissioner's determination (R. 64a) and the Circuit Court of Appeals affirmed the Tax Court's decision (R. 73–74).

ARGUMENT

1. The decision below is not in conflict with any decision of this Court or of an inferior appellate court. The petitioner does not claim that there is a conflict in the ordinary sense of the term, but only in that the "liberal" construction of a portion of the statute, to which the court below

is said to have resorted in arriving at its conclusion here, is inconsistent with the "strict" construction which this Court is said to have placed upon other portions of the statute in arriving at the conclusions it did in the cases of *Mother Lode Co.* v. *Commissioner,* 317 U. S. 222, and *Riley Co.* v. *Commissioner,* 311 U. S. 55.

Thus the petitioner contends that if, instead of "liberally" construing the provisions of Section 114 (b) (4) which were added thereto by the 1936 Act (Appendix, *infra,* pp. 12–13), the court below had construed them "literally," as this Court is said to have construed the other provisions of the section in both of the cited cases, the court below would necessarily have reached the conclusion that the petitioner was entitled to a new election to take percentage depletion in 1936 under the 1936 Act, even though it may, in view of the decision of this Court in the *Mother Lode* case, have been required, but failed, to make such election in 1934 under the 1934 Act.

This contention presents nothing for review.

2. There is, moreover, no basis for the petitioner's contention that the court below improperly construed Section 114 (b) (4) of the Revenue Act of 1936 as requiring the taxpayer to adhere to the election it negatively made in 1934 under Section 114 (b) (4) of the 1934 Act (Appendix, *infra,* pp. 11–12) by its failure then to elect percentage depletion.

By Section 114 (b) (4) of the Revenue Act of 1932, c. 209, 47 Stat. 169, Congress inaugurated a new policy regarding the basis for deductions on account of depletion in the case of metal, coal, and sulphur mines. Under that section, a taxpayer was privileged in the years 1932 and 1933 to have the greater of (1) the percentage depletion allowance, or (2) an allowance computed on the adjusted basis provided by Section 113 (b), commonly referred to as the cost basis. In its taxable return for 1933, however, the petitioner was required to make an election for 1934 which was binding upon it for all subsequent years. The only election required to be made expressly was the election to take the deduction on the percentage basis. If it failed to make such election it was deemed to have elected to take the deduction on the cost basis. S. Rep. No. 665, 72d Cong., 1st Sess., p. 30 (1939–1 Cum. Bull. (Part 2) 496, 518); also Article 225 of Treasury Regulations 77, promulgated under the 1932 Act.

The 1934 Act, however, required a new election for 1934 and all subsequent years, so that an election to take percentage depletion made for the first time in 1935 was held to be *functus officio* where the taxpayer in 1934 had had items of gross income, even though he had no net income. For in the *Mother Lode* case this Court held that the election to take percentage depletion must, in such circumstances, have been made in 1934, and that

failure then to make such election constituted an election to take depletion thereafter without reference to percentage depletion. Hence, unless the 1936 Act gave the petitioner a new election, the 1934 election of cost depletion, negatively made by the petitioner's failure affirmatively to elect percentage depletion, would control.

Section 114 (b) (4) of the 1936 Act is identical with the provisions of Section 114 (b) (4) of the 1934 Act, except that the following sentence was added to the section by the 1936 Act:

> The above right of election shall be subject to the qualification that this paragraph shall, for the purpose of determining whether the method of computing the depletion allowance follows the property, be considered a continuation of section 114 (b) (4) of the Revenue Act of 1934, and as giving no new election in cases where such section would, if applied, give no new election.

This sentence, in identical language, also appears in Section 114 (b) (4) of the 1938 Act, which likewise is otherwise identical with Section 114 (b) (4) of the 1934 Act. The same is true of Section 114 (b) (4) of the Internal Revenue Code.

It is thus at once apparent that, but for the addition of this sentence, a new election would have been permitted under both the 1936 and 1938 Acts. Cf. *Mother Lode Co.* v. *Commissioner, supra.* The question then is whether the

provision of the added sentence prohibits a new election in any taxable year to which either the 1936 or the 1938 Act applies, where it appears that an election should have been made in a prior year to which the 1934 Act was applicable. We submit that the added sentence does prohibit a new election in such a case.

The obvious purpose of Congress in enacting Section 114 (b) (4) of the 1934 Act was to provide a method of computing depletion allowance which would follow the property in all years to which that Act might be applicable, so long, but only so long, as it remained in the hands of the taxpayer who was required to make the election. Moreover, such an election was to be made in the first year to which the Act applied in which an election could be made thereunder. In the case at bar, this was the year 1934.

It was in order to carry out that policy thereafter, regardless of the enactment of new revenue acts, which normally became effective only in the respective years of their enactment, that Congress added the new sentence to Section 114 (b) (4) in the Revenue Act of 1936, and that it later included the sentence in Sections 114 (b) (4) of the 1938 Act and the Internal Revenue Code. We do not see how the language used could be clearer than it is to carry this purpose into effect; and so the court below appears to have thought when it said that this was the

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common sense construction of the statute. Indeed, in the case of *Tonopah Mining Co.* v. *Commissioner,* 127 F. (2d) 239, 244, it had already concluded that any other construction would be absurd.

The petitioner does not say what its view of the purpose and meaning of the added language is. But, if it is not to deny a new election to a taxpayer who continues in ownership or possession of the property, it could only be to deny a new election to a taxpayer who initiates ownership in a taxable year to which either the 1936 or the 1938 Act or the Internal Revenue Code is applicable. Although not made here, this contention was made by the petitioner below. It was rejected by the court below on the authority of the *Tonopah* case, as has already been indicated, because the result which its acceptance would achieve was absurd.

Moreover, to construe the added language as inapplicable to a continuing owner is but to require a disregard of the addition in its entirety; for the continuing owner would, as has been pointed out, have been permitted a new election in 1936 under the 1936 Act if the sentence in question had not been added thereto.

We submit that the petitioner's contention is not deserving of this Court's consideration.

3. In any event, the question here presented is moot. The petitioner cannot prevail even if it was permitted to make a new election under Section 114 (b) (4) of the 1936 Act. For, if it was permitted, it was likewise required to do so. And, if it was required to make a new election under Section 114 (b) (4) of the 1936 Act for the years 1936 and 1937, it was likewise required to make a new election under the identical language of Sections 114 (b) (4) of the 1938 Act and the Internal Revenue Code for the years 1938 and 1939, respectively. The election in 1936, upon which it relies, would not be sufficient. But the record does not disclose that the petitioner made such an election in 1938, although it does disclose, and there is no denial here, that it had gross income in that year (R. 12a–16a).

4. Furthermore, the question which the petitioner here presents is no longer of any importance, for by Section 145 of the Revenue Act of 1942, c. 619, 56 Stat. 798, Section 114 (b) (4) of the Internal Revenue Code was amended so as to permit an election to be made to take percentage depletion each year for any taxable year beginning after December 31, 1941.

CONCLUSION

There is no conflict. The contentions advanced are not meritorious. As concerns this petitioner,

the question is moot, and it is in any event of no importance in view of the 1942 amendment of the statute. For these reasons, the petition should be denied.

Respectfully submitted.

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SEPTEMBER 1944.

APPENDIX

Revenue Act of 1934, c. 277, 48 Stat. 680:

SEC. 114. BASIS FOR DEPRECIATION AND DEPLETION.

* * * * *

(b) *Basis for Depletion.*—

(1) *General rule.*—The basis upon which depletion is to be allowed in respect of any property shall be the adjusted basis provided in section 113 (b) for the purpose of determining the gain upon the sale or other disposition of such property, except as provided in paragraphs (2), (3), and (4) of this subsection.

* * * * *

(4) *Percentage depletion for coal and metal mines and sulphur.*—The allowance for depletion under section 23 (m) shall be, in the case of coal mines, 5 per centum, in the case of metal mines, 15 per centum, and, in the case of sulphur mines or deposits, 23 per centum, of the gross income from the property during the taxable year, excluding from such gross income an amount equal to any rents or royalties paid or incurred by the taxpayer in respect of the property. Such allowance shall not exceed 50 per centum of the net income of the taxpayer (computed without allowance for depletion) from the property. A taxpayer making his first return under this title in respect of a property shall state whether he elects to have the depletion allowance for such property for the taxable year for which the return is made computed with or without regard to percentage depletion, and

the depletion allowance in respect of such property for such year shall be computed according to the election thus made. If the taxpayer fails to make such statement in the return, the depletion allowance for such property for such year shall be computed without reference to percentage depletion. The method, determined as above, of computing the depletion allowance shall be applied in the case of the property for all taxable years in which it is in the hands of such taxpayer, or of any other person if the basis of the property (for determining gain) in his hands is, under section 113, determined by reference to the basis in the hands of such taxpayer, either directly or through one or more substituted bases, as defined in that section.

Revenue Act of 1936, c. 690, 49 Stat. 1648:

SEC. 114. BASIS FOR DEPRECIATION AND DEPLETION.

* * * * *

(b) *Basis for Depletion.*—

(1) *General rule.*—The basis upon which depletion is to be allowed in respect of any property shall be the adjusted basis provided in section 113 (b) for the purpose of determining the gain upon the sale or other disposition of such property, except as provided in paragraphs (2), (3), and (4) of this subsection.

* * * * *

(4) *Percentage depletion for coal and metal mines and sulphur.*—The allowance for depletion under section 23 (m) shall be, in the case of coal mines, 5 per centum, in the case of metal mines, 15 per centum, and, in the case of sulphur mines or deposits, 23 per centum, of the gross income from the

property during the taxable year, excluding from such gross income an amount equal to any rents or royalties paid or incurred by the taxpayer in respect of the property. Such allowance shall not exceed 50 per centum of the net income of the taxpayer (computed without allowance for depletion) from the property. A taxpayer making his first return under this title in respect of a property shall state whether he elects to have the depletion allowance for such property for the taxable year for which the return is made computed with or without regard to percentage depletion, and the depletion allowance in respect of such property for such year shall be computed according to the election thus made. If the taxpayer fails to make such statement in the return, the depletion allowance for such property for such year shall be computed without reference to percentage depletion. The method, determined as above, of computing the depletion allowance shall be applied in the case of the property for all taxable years in which it is in the hands of such taxpayer, or of any other person if the basis of the property (for determining gain) in his hands is, under section 113, determined by reference to the basis in the hands of such taxpayer, either directly or through one or more substituted bases, as defined in that section. The above right of election shall be subject to the qualification that this paragraph shall, for the purpose of determining whether the method of computing the depletion allowance follows the property, be considered a continuation of section 114 (b) (4) of the Revenue Act of 1934, and as giving no new election in cases where such section would, if applied, give no new election.

The provisions of Sections 114 (b) (1) and (4) of the Revenue Act of 1938, c. 289, 52 Stat. 447, and the Internal Revenue Code are identical with those of the corresponding section of the 1936 Act.

Treasury Regulations 86, promulgated under the Revenue Act of 1934:

> ART. 23 (m)–5. *Computation of depletion based on a percentage of income in the case of coal mines, metal mines, and sulphur mines or deposits.* * * *
>
> In his first return made under Title I of the Act (for a taxable year beginning after December 31, 1933) the taxpayer must state as to each property with respect to which the taxpayer has any item of income or deduction whether he elects to have the depletion allowance for each such property for the taxable year computed with or without reference to percentage depletion. An election once exercised under section 114 (b) (4) and this article cannot thereafter be changed by the taxpayer, and the depletion allowance in respect of each such property will for all succeeding taxable years be computed in accordance with the election so made. If the taxpayer fails to make such statement in the return in which the election should be so indicated, the depletion allowance for the year for which an election must be first exercised and for all succeeding taxable years will be computed without reference to percentage depletion. The method, determined under section 114 (b) (4) and this article, of computing the depletion allowance shall be applied in the case of the property for all taxable years in which it is in the hands of such taxpayer,

or of any other person if the basis of the property (for determining gain) in his hands is, under section 113, determined by reference to the basis in the hands of such taxpayer, either directly or through one or more substituted bases, as defined in that section.

Treasury Regulations 94, promulgated under the Revenue Act of 1936:

ART. 23 (m)–5. *Computation of depletion based on a percentage of income in the case of coal mines, metal mines, and sulphur mines or deposits.*—* * *

Subject to the qualification specified in the last sentence of this paragraph, a taxpayer making his first return under Title I of the Act (for a taxable year beginning after December 31, 1935) in respect of a property must state as to each such property whether he elects to have the depletion allowance for each such property for the taxable year computed with or without reference to percentage depletion. For the purpose of this article the taxpayer's first return under Title I of the Act in respect of a property is the return made under that title for his first taxable year (beginning after December 31, 1935) for which he has any item of income or deduction with respect to such property. An election once exercised under section 114 (b) (4) and this article can not thereafter be changed by the taxpayer, and the depletion allowance in respect of each such property will for all succeeding taxable years be computed in accordance with the election so made. If the taxapayer fails to make such statement in the return in which the elec-

tion should be so indicated, the depletion allowance for the year for which an election must be first exercised and for all succeeding taxable years will be computed without reference to percentage depletion. The method, determined under section 114 (b) (4) and this article, of computing the depletion allowance shall be applied in the case of the property for all taxable years in which it is in the hands of such taxpayer, or of any other person if the basis of the property (for determining gain) in his hands is, under section 113, determined by reference to the basis in the hands of such taxpayer, either directly or through one or more substituted bases, as defined in that section. The right of election specified in this paragraph is subject to the qualification that section 114 (b) (4) shall, for the purpose of determining whether the method of computing the depletion allowance follows the property, be considered a continuance of section 114 (b) (4) of the Revenue Act of 1934, and as giving no new election in cases where such section would if applied, give no new election.

The provisions of article 23 (m)–5 of Treasury Regulations 101, promulgated under the Revenue Act of 1938, and Section 19.23 (m)–5 of Treasury Regulations 103, promulgated under the Internal Revenue Code, are substantially the same as those contained in Article 23 (m)–5 relating to the 1936 act.

U. S. GOVERNMENT PRINTING OFFICE: 1944